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NO. 89-617

IN THE SUPREME COURT OF
THE UNITED STATES

October Term, 1989

TEXARKANA NATIONAL BANK
Petitioner

vs.

THE FEDERAL DEPOSIT INSURANCE CORPORATION,
in its corporate capacity as liquidator of
Guaranty Bond State Bank
Respondent

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

REPLY BRIEF FOR THE PETITIONER

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ARGUMENT

Respondent asserts in its brief that the judgment of the Court of Appeals can be upheld based upon the supposed lack of due care of Petitioner in purchasing the loan participations from Guaranty

Bond State Bank ("GBSB"). Resp. 12-13. In doing so, Respondent reasserts its contention, first made to the Court of Appeals, that Petitioner ignored "red flags" regarding the "suspect" nature of the Bell and Gunther loans and failed to conduct a "routine" credit check. Respondent's contentions are contrary to the facts in this case and the law applicable to those facts, and, as such, are without merit.

The district court, which had an opportunity to hear and view all of the evidence and to judge the veracity of the witnesses, entered its finding that Petitioner's reliance on GBSB's misrepresentations was "justified". Pet. App. 22b. Although FDIC challenged this finding at the Court of Appeals, that Court did not overturn the district court's finding. However, Judge Williams, in his dissent, examined

the evidence at trial and concluded that the trial court's finding in this regard was "not clearly erroneous" and that Petitioner's practice in handling the Bell and Gunther loan participations "was reasonable". Pet. App. 37a-41a.

When viewed in context, the facts of this case abundantly support the trial court's findings. First, the parties in this case had numerous prior business dealings. The Petitioner participated in at least fourteen other loan participations originated by GBSB Pl. Ex. 18-29, 32, Def. Ex. A-20. By FDIC's own admission, the underlying loans from all these other participations were valid and paid in full. Tr. 83. Further, when GBSB approached Petitioner to participate in the Bell and Gunther loans, GBSB supplied Petitioner with supporting documentation. This written

documentation included the loan instruments, security agreements, and financing statements (all purportedly signed by Bell and Gunther and signed by officers of GBSB), collateral inspection certificates signed by GBSB's President, and the purported financial statements of Messrs. Bell and Gunther. Testimony revealed that these documents were required before the purchase of the loan participations could be approved. Pl. Ex. 30-31, Tr. 170-175, 193. Petitioner depended on the written statements of GBSB's president contained in those documents, just as it would have the statements of the presidents of banks in Dallas and Little Rock, with which it had loan participations. Tr. 193-194. Finally, Petitioner had never had occasion to believe that GBSB's President had attempted to sell a participation in a nonexistent loan. Tr.

194. It therefore had every right to assume that GBSB was competent to conduct its own affairs. See, Barclays Bank D.C.O. v. Mercantile National Bank, 481 F.2d 1224, 1235 (5th Cir. 1973), cert. dismissed, 414 U.S. 1139, 94 S.Ct. 888, 39 L.Ed.2d 96 (1974).

Thus, Petitioner exercised reasonable care and diligence in requiring the written supporting documentation of the Bell and Gunther loans. It also acted reasonably in relying on the written representations and statements of the officers of GBSB, a bank with which it had numerous prior dealings. Traylor v. Gray, 547 S.W.2d 644 (Tex. Civ. App. - Corpus Christi 1977, writ ref'd n.r.e.); Long v. Smith, 466 S.W.2d 32 (Tex. Civ. App. - Corpus Christi 1971, writ ref'd n.r.e.). In addition, since there was seemingly nothing out of the ordinary in this

transaction, Petitioner acquired no knowledge of any facts which would put it on inquiry and impose upon it a duty to make an investigation to discover the existence of fraud. Thus, Petitioner's practice in purchasing the Bell and Gunther loan participations was reasonable and it had no duty to make further inquiry since the law does not require such an inquiry "where there is no reason to be suspicious and there is no negligence." Traylor, at 653. See also Cooper Petroleum Co. v. LaGloria Oil and Gas Co., 436 S.W.2d 889 (Tex. 1969). Pet. App. 38a-40a.

Even though Petitioner's practice and procedure in regard to the Bell and Gunther loan participations were reasonable and there was nothing out of the ordinary in this seemingly routine commercial transaction, FDIC imagines, with the aid of perfect hindsight,

certain "red flags" that were allegedly ignored by Petitioner. Resp. 13. First, FDIC finds a "suspicious nature" in the participations because they were "round-number offerings". Although FDIC does not elaborate on why a "round-number offering" is suspect, it is obvious that there is nothing per se suspect when one bank offers a "round-number" loan participation to another bank with which it has had numerous dealings. The facts also belie FDIC's imagined suspect nature of the "round-number" offering. Of the thirteen other loan participations involved in this suit, twelve were "round-number" offerings, including a $120,000.00 participation in a loan to Freeman Nurseries, Inc. Pl. Ex. 18-29, 32. All of these loan participations were valid and the underlying loans were eventually paid by the makers according

to their terms. Tr. 83. Thus, neither in the abstract nor within the context of the business dealings between Petitioner and GBSB, did Petitioner have any reason to be suspect because of the "round-number" offerings of the Bell and Gunther loan participations.

FDIC next contends that the size of the participations was "unprecedented" and therefore "suspect". However, there is nothing in the size of the Bell and Gunther participations which is "suspect". There is no testimony that the amount of these loan participations was in any way extraordinary or unusual for a bank the size of GBSB. The evidence at trial shows that Petitioner participated in loans made to James S. Carlow by GBSB in the aggregate amount of $88,000.00. Pl. Ex. 19-23. Further, Petitioner purchased a participation in a loan to Freeman Nurseries from GBSB in

the amount of $120,000.00, one week before GBSB's failure. Pl. Ex. 32. All of these loans were valid and paid in full. Therefore, there was nothing in the size of the Bell and Gunther participations which could be characterized as "red flags" since they were neither "unprecedented" nor unusual.

Finally, the FDIC imagines negligence on the part of Petitioners by its failure to make a "simple phone call to the borrowers". Resp. 13. Once again, in its attempt to find wrong doing on the part of Petitioner, FDIC ignores the facts of this case, the law applicable to those facts and the ordinary business practices of banking institutions. First, as has been seen, from all appearances this transaction was a normal business transaction between parties with a long history of

prior business dealings. The subject transaction and the method of dealing between Petitioner and GBSB was no different than the way the parties had dealt in prior transactions. Also, Petitioner dealt with GBSB in the same manner as it dealt with banks in Little Rock, Dallas, and other places. Under these facts, Petitioner had no reason to be suspicious, and thus had no duty to make a "simple" phone call to the borrowers. Traylor, supra at 653.

Further, the phone call to the borrowers in the context of a loan participation would be far from "simple". In a typical loan participation transaction, the borrower is unaware that his loan may be "sold" to participating banks, or the identity of those participating banks. In many instances, the participating bank may be one with which he does not want to do

business. Direct contact by the participating bank, as advocated by FDIC, to verify the borrower's loan and supporting documents could seriously erode the customer's confidence in the originating bank and endanger that bank's relationship with its customer. This, in turn, would have a severe impact on the relationship between the originating and participating banks. In this context, a phone call to the originating bank's borrower would be highly unusual and could have potentially disastrous results.

Finally, this "simple" phone call goes far beyond the standards embodied in the Comptroller of the Currency's recently published policy regarding loan participations. See OCC Policy Guidelines, 4 Fed. Banking L. Rep. (CCH)

Paragraph 60,799, at 38,858.[1] Although the guidelines call for an agreement by the borrower to make full credit information available to the originating bank, which is to provide that information to the participating bank, there is nothing in the guidelines which can reasonably be construed to require direct contact by the participating bank with the originating bank's customer. FDIC's position, therefore, goes far beyond the guidelines it seeks to incorrectly and retroactively impose upon Petitioner.

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[1] Although FDIC asserts that this policy is "longstanding", it is significant that these guidelines were not issued until August 3, 1984, over two years after the transactions involved in this case. They were issued because of "recent abuses" in the sale of loan participations. 4 Fed. Banking L. Rep. (CCH) Paragraph 60,799 at 38,858-38,859. As such, these guidelines cannot be used to judge the actions of Petitioner in a transaction arising before these "recent abuses" necessitated the issuance of these guidelines.

Thus, the facts of this case shows that Petitioner exercised prudent lending practices in its purchase of the Bell and Gunther loans and supports the trial court's finding that Petitioner's actions were justifiable or reasonable. As such, it was not negligent in its purchase of these participations and cannot be said to have participated in any way in GBSB's President's fraudulent scheme.

CONCLUSION

For all the reasons stated above and in the Petition for Writ of Certiorari, this Court should issue a Writ of Certiorari to review the opinion and judgment in the Fifth Circuit Court of Appeals with respect to its holding that D'Oench, Duhme & Co. v. FDIC, 315 U.S. 447, 62 S.Ct. 676, 86 L.Ed. 956 (1942) as codified in 12 U.S.C. § 1823(e) bars Petitioner from

asserting its setoff of the Bell and Gunther loan participations.

Respectfully submitted,

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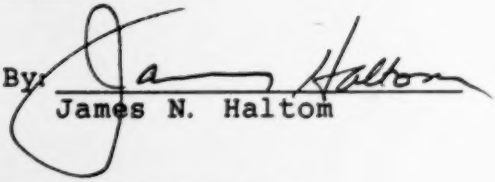
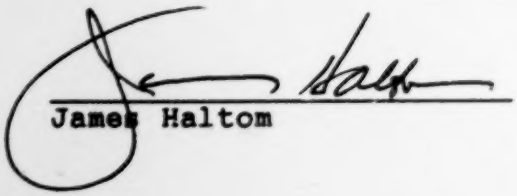
By: 
James N. Haltom

CERTIFICATE OF SERVICE

I hereby certify that three (3) true and correct copies of the foregoing Reply Brief for Petitioner were forwarded on January 5, 1990, by United States Mail, postage prepaid, to Mr. Kenneth W. Starr, Solicitor General, Department of Justice, Washington, D.C., 20530 and to Mr. T. Ray Guy, Respondent's attorney at the Fifth Circuit, Jenkins, & Gilchrist, 3299 Allied Bank Tower, Dallas, Texas 75202-2711.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